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"On-the-Spot" Survey #1

 PN-ACZ-747

MEMORANDUM FOR MEMBERS OF THE WORKING GROUP ON SPECIAL
SENATE STUDIES OF THE FOREIGN AID PROGRAM

FROM: O/Assistant to the Director for Congressional
Presentation

RE : An "On-the-Spot" Survey in Portugal, Spain, France, Italy,
United Kingdom and NATO - by former Ambassador Jefferson Caffery

Attached are a copy of a covering note to the Special Senate Committee and a series of recommendations by the former Ambassador Caffery on each subject item above. A copy of this report has been sent by Mr. Carl Marcy, Chief, Senate Foreign Relations Committee Staff, to the Department of State for clearance, which in turn, has loaned its copy to ICA.

The report itself is being circulated to the ICA Regional Offices for necessary comment and preparation of a position paper where necessary.

Attachments

FA:dm

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BY COWEN SEP/MD/CRM
AUTHORITY: EO 12065 & para 923, Uniform Security
Regulations


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BEST AVAILABLE

December 27, 1956

FOR THE SPECIAL SENATE COMMITTEE TO STUDY THE
FOREIGN AID PROGRAM

The Russians are definitely dedicated to taking over the world and to that end they change their tactics to suit their own convenience, not ours. We must not be misled by them. It would be tragic for us to indulge in too much wishful thinking regarding Russian domestic difficulties. Difficulties exist, but there is no evidence that Russian military might has been weakened in any appreciable way.

The only real deterrent to the destruction of the United States by the Russians or to their domination of the world is an adequate supply of nuclear bombs and the capacity to deliver them. This involves also, at this juncture, the maintenance in Great Britain, France, Spain, Italy and elsewhere of adequate forward air-bases; and NATO.

We must bear in mind that we could not sit quietly by and see the destruction or occupation of Western Europe by the Soviets. Were NATO not present, and, above all, were we not present in NATO, the Russians could easily take over Western Europe. Were Western Europe taken over by the Russians, far-reaching and very adverse consequences in every field would be in store for us. We would be forced into isolation whether we liked it or not and under the most disadvantageous circumstances.

When European prosperity suffers, ours is eventually affected too; and that is one reason why we cannot be indifferent to the consequences on the economy of Western Europe of the recent most ill-advised Suez adventure.

And this is equally true when we face the unfounded criticisms in the United Kingdom and France of our attitude during recent United Nations meetings at New York, following upon the disastrous Suez adventure. It would have

been folly for us to vote in any other way and in the long run France and the United Kingdom will come to realize this too.

This is even true in the face of the fact that American aid is often simply taken for granted.

Also were the nations in Western Europe to collapse economically, NATO would collapse too and we would be left on our isolationist own.

Nevertheless, for reasons which emerge in my reports regarding Italy, France, Portugal and Great Britain, I do not at this time recommend direct economic grant aid to any of those countries nor do I recommend at this time aid allocations to their military budgets.

In my reports on each of these countries, I do make specific recommendations as to whether or not certain other forms of aid should be continued.

I point out that in view of the consequences of the Suez operation, it is possible that we may be impelled at some future date to take a New Look at the economic and military aspects of the situation in Italy, France, Great Britain, Portugal and Spain.

In my opinion, the aid programs in general have been efficiently administered, although it would be easy enough to pick flaws here and there, but on the whole, it has been a case of value received. Without such aid, there exists the real possibility that the Iron Curtain would now be on the shores of the Atlantic.

I treat Spain apart from the NATO countries.

I submit reports on:

1. France
2. Italy

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3. Portugal
4. Post-Suez United Kingdom
5. NATO
6. Spain

Jefferson Caffery
Rome, Italy
January 9, 1957

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FRANCE - RECOMMENDATIONS

1. I do not recommend at this time any additional economic aid.
2. In the case of OSP (Offshore Procurement), in the future this program should be considered only in exceptional circumstances such as
 - a. clearly established military justification, or
 - b. where there are genuine cases of economy, or
 - c. where there are especial political problems.
3. I consider that the nature of the Labor and Communist problems is such as to make the continuation of a labor exchange program for several years desirable.
4. I do not recommend at this time any new aid allocations in support of the military budget.
5. I recommend a continuance of the Agricultural Sales Programs.
6. I recommend that we should continue to program military end-item aid for France in the form of modern weapons but not including at this particular juncture nuclear warheads, plus certain limited amounts of spares and replacements for equipment not produced in France.
7. Every issue has been tremendously complicated by the invasion of Egypt. The high degree of French dependence for crude oil (roughly 85%) upon the Suez and the IPC pipeline will cause serious troubles. Nevertheless, France is in a position to withstand a short period in which the Canal and the pipeline from Iraq cannot be used.

Over a longer period, however, real difficulties will emerge, although her foreign exchange resources would allow her to absorb the dollar costs for a period of time. To indicate the magnitude of this dollar exchange problem

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France, Recommendations

alone, it is estimated that if this condition continued to exist during the first six months of 1957, the direct additional dollar drain could amount to \$100 million to meet even a reduced level of requirements. As the Bank of France gold reserves and foreign exchange amount to \$1.2 billion, this could be absorbed - if this were the only substantial drain.

The politico-economic effects, however, go much deeper. Even before the petroleum crisis, the balance-of-payments was already running a heavy deficit under the pressures of inflation, the costs of the Algerian campaign, and the cold spell of last winter. France, in common with many other European countries, faces a serious inflationary danger under conditions of full employment. Use of shipping around the Cape and obtaining petroleum from the Western Hemisphere will increase costs considerably. Presumably such increase could, and probably would, be absorbed by the government budget in the form of increased expenditures for price subsidies. This, in turn, however would contribute to the budgetary deficit, which, in itself, is a major inflationary factor in France.

Even assuming utilization of dollar reserves to pay the dollar cost, and budgetary funds to subsidize the increase costs, there is no doubt but that actual imports and available supplies would be reduced. In France's overextended economy, which is characterized by a shortage of energy, this condition, together with other economic pressures, could result in major inflationary developments early in 1957.

Today, it is impossible with any assurance even to state the assumptions on which the French economy will have to operate in 1957. It can, however, be

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France, Recommendations

definitely stated that if the Canal and the pipeline remain closed until the middle of 1957, the French economy will be faced with economic and financial problems which France alone is unlikely adequately to resolve.

The effect of serious inflationary developments in France upon the local political scene and France's international position, to say nothing of its contribution to NATO, appear too obvious to require comment.

Therefore, we may be compelled later on to take a New Look at the situation in France.

8. I recommend that we should urge the French to take forthright action designed to bring their economic position into balance.

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ITALY - RECOMMENDATIONS

1. I do not recommend at this juncture direct economic grant aid to Italy. Appropriate loans, use of counterpart currency, technical assistance for economic development and private investments can be recommended. I particularly recommend that we should continue the program of sale of Surplus Agricultural Commodities under Public Law 480, Title I and the Child Feeding Program under Title II and Relief under Title III. The USOM should be phased out and its work integrated with the Embassy Economic Section. F?

2. I do not recommend at this time aid allocations to the Italian Military Budget.

3. I do recommend that we should continue to program certain selective end-item military aid for Italy, notably in the form now of dual purpose weapons (But not including at this particular juncture nuclear warheads), plus certain limited amounts of spares for equipment not produced in Italy and a continuance of the present limited program of maintenance assistance.

4. In the case of Italy, whenever, and if it suits our purpose, we might take on a renewed interest in Offshore Procurement.

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PORTUGAL - RECOMMENDATIONS

1. I do not recommend any changes in present objectives, type and magnitude of our Aid Programs in Portugal.
2. I do recommend an appropriate phased program of end-item aid in the form of dual purpose weapons but not including, at this particular juncture, nuclear warheads.

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UNITED KINGDOM - RECOMMENDATIONS

1. I do not recommend any new direct military or economic grant aid to the United Kingdom at this juncture.

2. I recommend that we should continue to program military hardware in the form now of dual purpose weapons, not including warheads at this juncture.

3. I recommend that we should continue a program of financing the export of surplus agricultural commodities.

4. I recommend a waiver of interest payments (\$81.6 million) due on the Anglo-American Financial Agreement.

5. The British would genuinely prefer to avoid further economic aid. They believe that their basic trading position is reasonably sound. They feel that the measures they are taking to curb inflation will work. They are pressing on with plans and programs to increase productivity. They are planning to enter a free trade area with Europe, with the consequent increase of competition with the rest of the world also. They are encouraged by the increase of trade with the dollar area. They firmly intend to solve their current balance-of-payments problems without resorting to reimposition of controls on imports from the dollar area. But they do feel that they must give primary emphasis to the improvement of their basic economic position which is indispensable to their survival. The burden of the defense effort as it now stands, seems to them more than they can continue to support.

This situation obviously calls for careful attention on the part of the United States and closer cooperation between the United States and the United Kingdom in the field of new weapons and research and development than has taken place in the past. A step in the right direction has already been taken in Secretary Wilson's proposals at the December meeting of the North Atlantic Council.

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6. Whether Britain's economic position will force cuts in her defense effort to an extent which would make it in the United States military interest to provide further military assistance cannot yet be determined. This is, however, a possibility which cannot be wholly excluded in our forward thinking. For it is clearly in the United States interest that the United Kingdom should continue and succeed in her effort to become and remain economically strong as a major free world partner of the United States over the long-term and also that the resources of capable military manpower and of geography which the U. K. provides should be deployed in the most effective possible manner in the common defense. In other words, at a future date, we may be compelled to take a New Look at the economic and military aspects of the situation in the United Kingdom.

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NATO - RECOMMENDATIONS

1. The coordinated defense effort must remain the heart of NATO but to sustain that defense effort it is essential to develop more political consultation and achieve more agreement among member countries. In other words, peoples and parliaments must come to have a sense of real participation in major political decisions affecting the Alliance as a whole, if they are to be persuaded to continue to shoulder heavy defense burdens. That does not mean, however, that the United States should be deprived of the right of independent action in areas, Latin-America for instance, and Formosa, outside of NATO's sphere. However, although the political, economic and cultural aspects of NATO are of much importance, they are of minor importance in relation to the importance of maintaining NATO's military strength. That military strength is the principal bulwark of the free world.

2. If NATO were to fall apart (in my considered judgment, there is no likelihood of that), the world this side of the Iron Curtain and particularly Western Europe would be severely shaken and we, in the United States, might be thrown on our isolational own in a truly frightening way, with a shrinking economy and the loss of our sense of security.

3. I recommend that we should continue to give NATO our full and effective support.

4. In my opinion, it is essential also to maintain NATO's maximum retaliatory strength, to increase deterrents to aggressions, having in mind that a nuclear war might be very short indeed.

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SPAIN - RECOMMENDATIONS

1. Our five major aid and naval bases and pipeline systems in Spain are considered by our competent authorities to be an essential part of our defense build-up against the Russian menace. Spain is one of the most outspoken anti-Communist nations.

2. This being so, it is in our own vital interest to see a viable Spain, economically as well as militarily. The objectives of the United States Program are to contribute to that end, but above all to support U. S. military programs in Spain.

(For various reasons and also principally on account of the controversial aftermath of the Spanish Civil War, Spain received no aid whatsoever from the United States until very recent years).

3. I recommend a continuance of the present program in Spain for military end-item equipment and related spare parts, as well as the Defense Support Program and the Program of U. S. Agricultural Sales and Grants under Public Law 480.

4. Crippling cold in early 1956 wiped out most of Spain's great citrus and olive crop, an estimated loss of about 20 percent of Spain's export earning. I consider justified the Spanish request for \$30,000,000 in additional aid for the current fiscal year to the end of June 30th for her Defense Support Program. The new funds are being sought under Section 401 of the U. S. Mutual Security Act. However, we should insist that the Spanish Government make serious efforts to control inflation.

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